

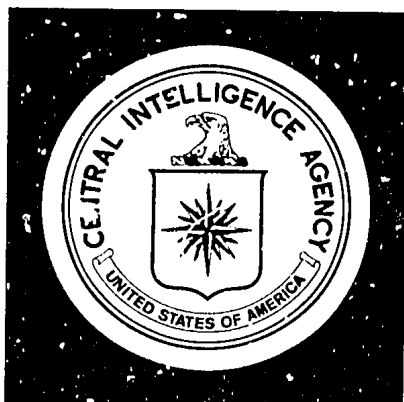
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# Economic Intelligence Weekly

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ER EIW 75-27

9 July 1975

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## ECONOMIC INTELLIGENCE WEEKLY

9 July 1975

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## Overview

Wage Demands in Three of the Six Major Foreign Economies Have Moderated in Recent Months Because of High Unemployment, Government Pressure, and Depressed Business Conditions.

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Unit labor costs have risen sharply in all the countries. While wages have continued to go up, productivity has been declining because of government aid and pressures to keep workers on payrolls despite sagging output. West Germany alone has avoided an appreciable decline in productivity.

Wholesale prices began to move up in April after falling for six months. Substantial inflation will continue in the months immediately ahead, with higher labor costs the predominant cause. Wage settlements already in train will cause further rises in unit labor costs because output and productivity will be slow to improve. As the expected increase in world production materializes toward the end of 1975, the pressures on costs will ease. At the same time, higher oil prices, almost inevitable in the fall, will give a new stimulus to the wage-price spiral.

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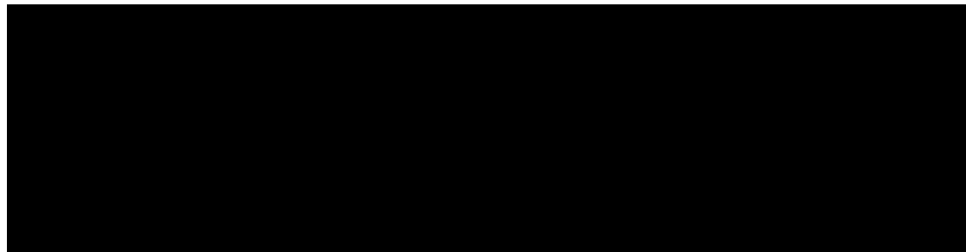
Note: Comments and queries regarding the *Economic Intelligence Weekly* are welcomed. They may be directed to [REDACTED] the Office of Economic Research, Code 143, Extension 5943.

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**The OECD High Level Group on Commodities Has Failed To Agree on Ways To Meet the LDC Demands** to be aired at the special session of the UN General Assembly this September. Debate followed expected lines:

- the French urged negotiation of international commodity agreements and the building of stockpiles;

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The group agreed to study marketing problems of copper, rubber, cocoa, tea, jute, and sugar, without committing the OECD countries to support of these markets.

**The French Franc Rejoins the Snake Thursday after Floating Freely for 18 Months.** At the same time, EC finance ministers will discuss several French suggestions for modifying the structure of the float. The ministers remain cool to most of these proposals, particularly that the range of the float against the dollar be narrowed. They may agree, however, to expand the short-term EC credit facilities that members can use to support the joint float. (Confidential)

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## Articles

### DEVELOPED COUNTRIES: WAGE-PRICE TRENDS

In spite of continuing global recession, progress in breaking the three-year old price spiral has stalled in most major foreign countries.

Wholesale prices have resumed their upward course for the first time in six months. The average rise in consumer prices in the Big Six, after easing in early 1975, has accelerated to an annual rate of 10%. While wage demands have been lower than anticipated in certain instances, stiff rises in labor costs will remain the predominant cause of inflation in the months immediately ahead.

#### Recent Price Trends

After declining substantially in early 1975, wholesale prices began moving up in April (as measured by three-month moving averages of seasonally adjusted data). Small increases occurred in West Germany and Italy, large ones in the United Kingdom and Canada. Japanese wholesale prices stabilized in April and May following nearly a six-month decline. Only in France have prices continued to fall.

The decline in wholesale prices had occurred largely because (a) demand was sluggish, with inventories building up, and (b) falling raw material prices were helping to offset large increases in labor costs. In the last few months, however, raw material prices have stabilized, while the upward trend in labor costs has continued. Faced with sharply reduced profit margins, industrial firms are no longer able to absorb the added costs.

The continued rise in consumer prices reflects mainly growing costs for food and services. On the average, increases in food prices since the start of 1975 have accounted for roughly one-half of the rise in consumer prices in the Big Six. Growth in prices for manufactured goods has tapered off to a 4% annual rate in recent months, reflecting the previous decline in wholesale prices. Prices of services, meanwhile, have continued to increase steadily.

#### Stubborn Labor Costs

Unit labor costs are still rising rapidly, even though extreme union demands have been checked in several countries. In the six major foreign countries, hourly wage rates in the first half of 1975 rose an estimated 16% (annual rate), compared

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with 20% in the second half of 1974. Unit labor costs have been increasing at 22% - faster than wage rates because of falling or stagnant production and government and union pressures to keep workers on payrolls.

#### Wage Rate Developments

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In Italy, wages rose 28% (annual rate) in the first quarter, compared with the same period of 1974, a rate that exceeds the record 1974 pace.

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[REDACTED]

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West Germany, France, and Japan have had more success in keeping their wage-price spiral under control.

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[REDACTED]

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in France, settlements since early 1975 have been running about 11%, down from 18% last year.

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[REDACTED]

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In all three countries, high unemployment, numerous bankruptcies, and a severe profit squeeze have undercut labor's bargaining position.

#### Outlook

Higher labor costs will remain the predominant cause of inflation in the months immediately ahead. Wage settlements already in train will push up unit labor costs considerably, because output and productivity will change little. In the meantime, business firms, their inventory position strengthened, will be better able to improve their unsatisfactory profit margins. Higher oil prices next October pose another inflationary threat. For every \$1 per barrel increase in oil prices, wholesale prices in the major countries generally rise by about one-half of one percent. (For Official Use Only)■

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[REDACTED]



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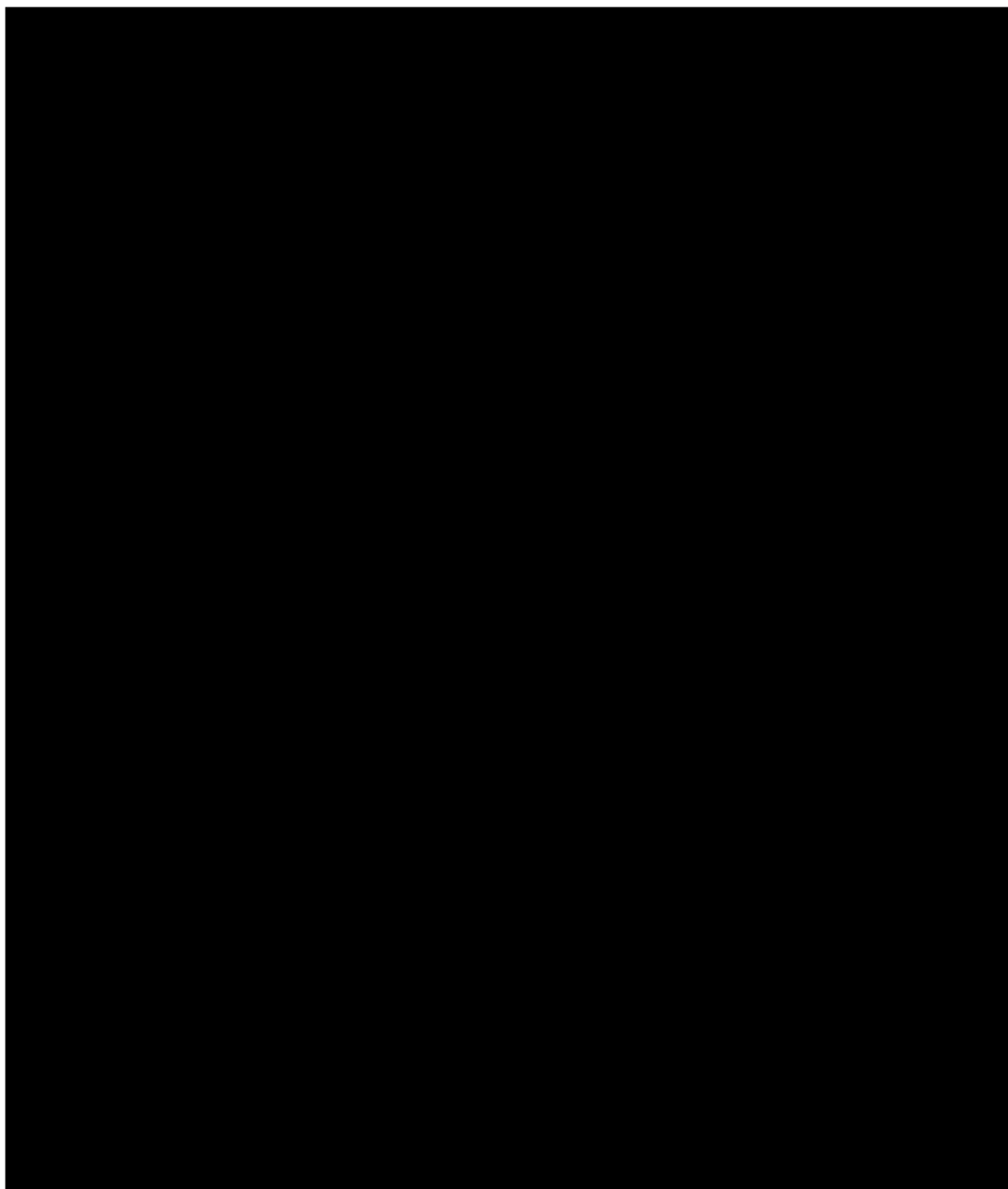
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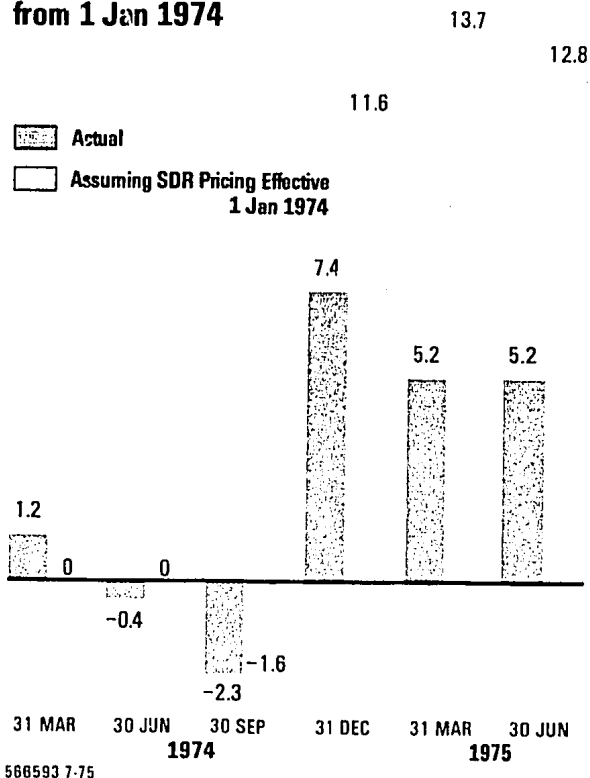
#### SDR OIL PRICING: DELAYING THE DECISION

Recent strength shown by the dollar may forestall a switch to SDR oil pricing on 1 October, even though OPEC members still profess an intention to adopt the new scheme.

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After reaching an apparent consensus in favor of the shift at the OPEC meeting in early June, some producers are now reconsidering. The impetus for SDR oil pricing stemmed from the dollar's weakness during 1974 and first half 1975. From the dollar's peak in January 1974 to June 1975, dollar depreciation reduced OPEC revenues by an average of \$160 million per month below revenues that would have been garnered under SDR pricing. OPEC members have repeatedly decried the decline of the dollar. Iran, Saudi Arabia, Kuwait, and Qatar cut the tie between their currencies and the dollar earlier this year, even though their international oil transactions continued to be denominated in dollars. SDR oil pricing, the next logical step, was discussed at the OPEC meeting in June and informally approved for adoption on 1 October.

# Percent Change in the Dollar Price of OPEC Oil from 1 Jan 1974



The recent strength of the dollar has modified some producer attitudes on the implementation of SDR oil pricing. In a recent statement, Iranian oil spokesman Amuzegar questioned whether OPEC would benefit from the shift, at least at this time. This and similar reservations by Kuwaiti spokesmen reflect a general cooling of OPEC officials toward the proposition. If the dollar continues to appreciate, OPEC countries will increase their revenues by staying with the present pricing system, over and above any gain from the anticipated price increase in October. (Secret) ■

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## IRAN: FEIGNING FINANCIAL WORRIES

At the Shah's instigation, government officials and the press are giving the impression that foreign aid and economic development efforts will have to be held down because of the decline in oil earnings in 1975. In fact, the Iranian balance of payments remains very strong. We believe that Tehran is using the drop in its oil revenues as an excuse to reject various aid requests and to raise oil prices.

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### The Shah's Move

In early 1975 the Shah directed his subordinates to stress the decline in oil revenues in turning down aid requests. This excuse was used in rebuffing requests for loans -- and for price concessions on oil purchases -- from a number of LDCs of little economic and political interest to Iran. Tehran told the IMF that it was considering a delay in making its full \$1 billion commitment to the oil facility, pending examination of the balance of payments later in the year. The Iranian press expanded the theme of financial woe by suggesting that cutbacks in economic development might be necessary.

### Balance-of-Payments Position

The balance-of-payments fears expressed by Iran are unwarranted. Although export earnings declined by 5% in the first half of 1975 compared with the previous half, they should pick up in coming months because of seasonal factors and the recovery in world economic activity. We believe that oil revenues will be only \$600 million lower in 1975 than in 1974, in contrast to the \$3.5-\$4 billion drop recently forecast by Minister of Interior Amuzegar. Even with imports rising 50% in value, we expect Iran to achieve a \$10 billion current account surplus in 1975.

Iran's lending and investments in 1975 probably will approach a record \$4.0 billion -- roughly double the 1974 level. About one-fifth is earmarked for the Communist countries of Bulgaria, Romania, and North Korea, where Iranian interest in acquiring raw materials meshes with a desire for improved political relations. The Shah's effort to gain more influence with the front-line Arab states is a major factor in aid flows to Egypt (forecast at \$250 million in 1975) and could bring badly needed assistance to Syria.

Loans to the French and British governments, together with investments in the French nuclear energy industry and in a West German machine tool and construction firm, will total well over \$1 billion in 1975. Loans to the IMF oil fund and purchases of IBRD bonds together will probably exceed \$1 billion; both offer attractive returns as well as political prestige for Iran.

Even with these outflows, Iran should rack up a payments surplus of \$6 billion in 1975, boosting foreign reserves to \$15 billion. (Secret No Foreign Dissem)■

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## INDIA: REFURBISHED ECONOMIC POLICIES

Prime Minister Gandhi is capitalizing on her state of emergency powers to show that the new political setup can advance Indian economic goals.

Sweeping new reforms have been announced, reminiscent of campaign pledges five years ago to abolish poverty. Price reductions for food and clothing top the priorities list. Merchants face tough new controls over prices and stocks and have lost much of their former judicial protection. These controls come at a time when crops are off to a good start and when wholesale prices have been stable for a few months. Prospects for short-term price reductions thus are good. Also promised are

- enforcement of existing land reforms laws;
- abolition of bonded labor and a moratorium on debts to village moneylenders;
- more grain and cheap cloth at government outlets; and
- cheaper food, housing, and books for students, who return to classes in July.

Discipline, hard work, and austerity are the watchwords of the new economic push. The fractious labor movement has been warned against any slackening in the work pace. Already bureaucrats and other public sector employees are showing up at work on time, and some reportedly have volunteered to work extra hours.

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Lax managers in the railway bureaus already have been sacked. Nevertheless, the government has neither marked out new directions in economic policy nor offered new investment programs to increase production. Well-publicized promises to increase irrigation by 5 million hectares, to expand electrical capacity by 2,600 megawatts, and to simplify the cumbersome business licensing system are rehashes of earlier government plans.

Gandhi's next initiative likely will involve strengthening central government control over economic affairs of the states. Indian law and political considerations have allowed the states to pursue agricultural and financial policies often at odds with national goals. State leaders, including those not members of the Congress

party, are expected to comply with commands so long as Gandhi maintains strict control. New Delhi for the moment has more clout in (a) settling longstanding interstate riparian disputes, (b) insuring proper spending of development funds, (c) forcing states to increase taxation of rich farmers, and (d) improving implementation of national agricultural policies, e.g., with respect to land tenure, grain procurement policies, and timely provision of fertilizer and other inputs. (Confidential)■

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### YUGOSLAVIA: BALANCE OF PAYMENTS WORSENS

A rapidly mounting trade deficit with the West has forced Belgrade to tighten import restrictions and seek debt relief. Recession in Western countries, EC restrictions on beef imports, and accelerating domestic inflation have depressed export earnings, while rapid economic growth continues to push up imports from the West.

#### Going Deeper into the Red

The trade deficit with convertible currency countries, mainly OECD members, climbed to an estimated \$1.5 billion in January-May 1975, compared with \$1.2 billion a year earlier. Remittances from workers abroad and earnings from tourism have not increased enough to cover the additional trade deficit. The \$220 million current account deficit in January-February was double the year-earlier figure. Belgrade's drawdown of its foreign exchange reserves by almost \$100 million in March and April indicates that the problem is continuing. By mid-June, reserves stood at \$1.3 billion, equivalent to 2-1/2 months' imports from the convertible currency area.

Belgrade has had to fall back on foreign reserves because credits are difficult to obtain. Several Western bankers say it has been practically impossible in recent months to place short-term Yugoslav paper in West European financial markets. Political considerations – an aging president and a possibly troublesome succession – are compounding the economic uncertainties. Last year, in contrast, Yugoslavia was able to borrow \$517 million in the Eurocurrency market, more than any other East European country.

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Yugoslavia: Foreign Trade

	Million US \$	
	Jan-May 1974	Jan-May 1975 <sup>1</sup>
Exports, total	1,536	1,650
Convertible currency area	1,024	1,000
East European and other clearing areas	512	650
Imports, total	2,833	3,250
Convertible currency area	2,186	2,500
East European and other clearing areas	647	750
Trade balance	-1,297	-1,600
Convertible currency area	-1,162	-1,500
East European and other clearing areas	-135	-100

1. Preliminary estimates.

Groping for Remedies

In May, Belgrade petitioned the IMF to defer until 1976 repayment of about \$25 million due the previous month. According to one source, Yugoslav officials also have requested postponement of at least part of the debt payment due West Germany in 1975.

To hold down foreign exchange outlays, Belgrade has begun requiring special permits for the import of 256 categories of investment and consumer goods during the remainder of 1975. The list is far broader than that instituted last summer and fall; it includes, for example, several types of machinery and equipment needed for energy production and raw materials development. Imports under long-term cooperation agreements do not require a special permit.

Meanwhile, the Yugoslavs apparently have launched a campaign aimed at shoring up the confidence of Western bankers. In a discussion with US bankers in late May, the Governor of the National Bank stated that Yugoslavia could avoid a further reduction in its foreign exchange reserves by drawing on the large credit extended by West Germany last year, by obtaining loans from Middle Eastern states, and by borrowing from the IMF and the World Bank, if necessary.

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### Prospects

Hard currency earnings probably will suffer through the remainder of 1975 at least, since the initial economic recovery in developed countries is expected to be slow. Before Belgrade imposed its recent import restrictions, the outlook was for a 1975 current account deficit in excess of the \$1.5 billion incurred last year. Senior financial officials indicate that the regime will continue to resist making sharp cuts in imports because of its political interest in maintaining economic growth and employment. As an alternative, Yugoslavia will shop for more of its imports in the USSR and Eastern Europe. Exports to the CEMA area – mostly consumer goods and other manufactures unsalable in the West – are larger this year than last. Yugoslavia thus far has drawn little of the \$540 million credit granted by the USSR in 1972.

The Yugoslavs claim to have covered at least two-thirds of the \$2.7 billion that we believe they will need to meet hard currency obligations (including debt service) in 1975. Sources of funds include the World Bank, the IMF oil facility, Exim Bank borrowing, commercial bank lines, supplier credits, and Eurodollar loans. Belgrade hopes that loans from the Middle East will help fill the gap. It may also seek additional selective debt rescheduling. If these approaches fail to provide sufficient funds, Belgrade will probably have to request a general rescheduling, as it did in 1971. (Confidential)■

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### Notes

#### Iran May Join Copper Group

Iran reportedly wants to join the Intergovernmental Council of Copper Exporting Countries (CIPEC) and probably will be admitted at the November meeting. Iran would be the first to join Chile, Peru, Zaire, and Zambia, which founded the organization in 1967. Other potential members – Australia, Papua/New Guinea, Indonesia, and the Philippines – so far have been reluctant to join. By 1977, Iran may produce as much as 150,000 tons a year. As a potential exporter, Iran will have a stake in high world market prices and could provide financial assistance to CIPEC price support schemes. (Confidential)

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**USSR: Grain Crop Update:**

Drought remained unbroken in the Volga Valley and Western Kazakhstan last week, killing most of the spring wheat in the area. [REDACTED]

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[REDACTED] winter wheat yields 10%-50% lower than last year. In most other areas, prospective yields range from good to excellent. We are preparing a new estimate of the total grain crop [REDACTED]

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[REDACTED] The new estimate will be a little lower than our June forecast of 215 million tons. [REDACTED]

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**Publications of Interest\***

**Egypt's Economic Transformation**

(ER IM 75-13, July 1975, Secret No Foreign Dissem)

This memorandum describes how Egypt, thanks to recent Saudi aid, will overcome the financial bind that threatened to impair economic growth in 1975. It also points up the factors for improved economic well-being over the next few years.

**Communist Aid and Trade Activities in Less Developed Countries, May 1975**

(ER RP 75-20, July 1975, Secret No Foreign Dissem)

The monthly report for May contains a summary of Communist economic and military aid activities in LDCs in 1974. Included is an annex detailing Communist-LDC trade in 1973.

\* Copies of these publications may be ordered by calling [REDACTED] Code 143, Extension 7234.

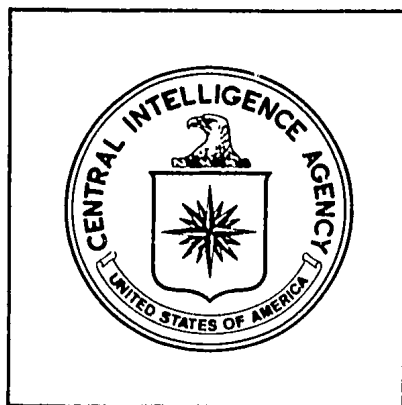
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**Foreign Trade Developments**

(ER FTD 75-1, July 1975. Secret No Foreign Dissem)

This new report, to be published periodically, has been initiated to provide economic intelligence in support of the Multilateral Trade Negotiations. It analyzes important trade trends, addresses trade issues, and provides policymakers with up-to-date information.



## *ECONOMIC INDICATORS*

Prepared by

The Office of Economic Research

July 9, 1975

### Foreword

The *Economic Indicators* provide up-to-date information on changes in the domestic and external economic activities of the major non-Communist developed countries. To the extent possible, the *Economic Indicators* are updated from press ticker and Embassy reporting, so that the results are made available to the reader weeks - or sometimes months - before receipt of official statistical publications.

Comments and queries regarding the *Economic Indicators* are welcomed. They may be directed to [REDACTED] the Office of Economic Research, Code 143, Extension 7402 or 351-7402.

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